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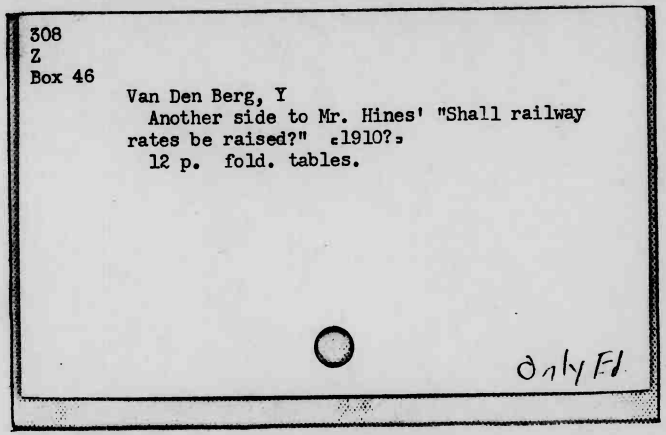

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Another Side to Mr. Hines'

"Shall Railway Rates Be Raised?"

BY

Y. VAN DEN BERG

Y. VAN DEN BERG
32 NASSAU STREET
NEW YORK

The question of Railroad Rates has become of vast public interest.

Mr. Walker D. Hines, Chairman of the Executive Committee of the Atchison, Topeka & Santa Fe Railway Company, contends, in substance, that rates must be advanced in order that Surpluses may be increased for the purpose of raising money with which to protect the railroads from depreciation or obsolescence and to improve and extend.

The facts set forth in the enclosed pamphlet are cited to prove that such course for the purpose stated is unsound, in conflict with the interests of the bona-fide Investors and the Public generally.

Another Side to Mr. Hines'
"Shall Railway Rates Be Raised?"

by

Y. VAN DEN BERG

The *Outlook* recently published an article by Mr. Walker D. Hines, Chairman of the Executive Committee of the Atchison, Topeka & Santa Fe Railway Company, under the title, "Shall Railway Rates be Raised?" in which he states in substance: that the A. T. & S. F. Railway, since it was reorganized fourteen and one-half years ago, to avoid obsolescence and to keep step with the spirit of progress, has expended for additional mileage about $65,000,000, and for Additions (largely Equipment) and Betterments to existing lines about $130,000,000, or a total of about $200,000,000—$50,000,000 of which was drawn from Surplus Earnings and $150,000,000 from the sale of Securities—and that to continue to protect the property from depreciation or obsolescence and to extend and improve it to meet the demands of the public, his company ought to raise and spend about $30,000,000 per annum for the next few years in addition to its current operating expenses—about $20,000,000 of which for additional and improved Equipment and for innumerable improvements to the existing lines, and about $10,000,000 for the construction of additional mileage.

He holds that as the property of the Santa Fe is already covered by First and Second Mortgages for

nearly $250,000,000, that source of raising new capital annually is virtually exhausted, and the only way to accomplish it is to sell stock or unsecured bonds or notes, or by drawing upon surplus earnings accumulated after interest on the bonds and reasonable dividends have been paid; but to be successful in selling stock one must pay dividends; to sell unsecured bonds or notes one must have credit; to have credit one must have surplus.

Mr. Hines favors the selling of unsecured bonds or notes and the drawing upon surplus earnings accumulated after interest on the bonds and reasonable dividends have been paid, and this, based upon actual experience, because the contribution out of surplus earnings, after interest charges have been met and dividends paid, materially facilitated the transaction of selling $115,000,000 of bonds convertible into stock.

The accumulation of surplus earnings, above fixed charges and dividends, to an extent sufficient to admit of contributions to Betterments from that source not less than one-fourth of the total money required, is also advocated on the ground that considerable of the expenditures due to the increasing demands of the Public are non-revenue producing and made for the promotion of comfort and gratification of æsthetic tastes (specific reference is made to the new Terminals at Kansas City), or for the protection of human life in the way of safety appliances and elevated instead of surface tracks (the demand for it is made by Wichita,

Kansas), and he concludes that as increased operating expenses, due to higher wages and prices, increased expense of public regulation, increased taxes, and after meeting the interest and dividend requirements threaten to diminish surplus earnings very rapidly, the condition cannot be adequately met except by a substantial increase in net revenues.

"The increasing burdens of operation make it imperative, the Company (Santa Fe) should have increased revenues if it is to fulfill the reasonable expectations of the public for the improvement and extension of the transportation service," and Mr. Hines adds that this is still more true of numerous roads less fortunate (in prosperity) than the Santa Fe has been, and whose transportation service calls for the expenditures of enormous amounts of additional capital in order to keep pace with increasing demands for improvements and extensions.

If it be kept in mind that Stockholders should realize dividends, what Mr. Hines says with respect to the bonded indebtedness of the Santa Fe, that source of raising new capital being virtually exhausted, is true to no less a degree of most of the railroads in this country, and hence it is also true that the only way to raise money for Betterments essential to protect the properties from depreciation or obsolescence, and to improve them to an extent as may be legitimately required in providing adequate facilities for the ever increasing

traffic of a growing and developing country is to draw upon surplus earnings or to sell additional stock or other non-fixed interest bearing Securities.

Many of our railroads have raised money for Betterments, etc., by selling additional stock or unsecured bonds convertible into stock or by borrowing in one way or another or otherwise, but that method of financing has not been universal and, to be specific, the Louisville & Nashville railroad is amongst the exceptions.

To make clear the two directly opposite policies and their effect it becomes necessary to cite certain facts, and these are conveyed in the tables appended hereto.

For present purposes, it will suffice to point out from those tables that the Santa Fe during the past ten years increased its mileage owned 48.82% (Table "A"), increased its cost of road and equipment, etc., 40.73% (Table "B"), and increased its capitalization outstanding in the hands of the public 44.83% (Table "C"). The Louisville and Nashville increased its mileage 45.55% (Table "A"); increased its cost of road, etc., 48.61% (Table "B"), and increased its capitalization in the hands of the public 29.06% (Table "C").

(Table "G"—a). In 1900, the density of the Santa Fe's freight traffic was in round figures 55 tons, and in 1910, 63 tons to the Louisville & Nashville 100 tons, and in both years it secured an average haul on this freight business of more than double the distance the L. & N. hauled its freight, and that, too, at an average

rate per ton for every mile hauled which in 1900 was 28.75%, and in 1910 35.15% greater than the L. & N. collected. Of passenger traffic (Table "G"—b) the Santa Fe in 1900 hauled 76 passengers and in 1910 119 passengers to the L. & N. 100, which it also carried more than double the distance the L. & N. did, collecting in 1900 an average of $1.94 and in 1910 an average of $1.86 from each passenger against the L. & N. 82 cents and 98 cents respectively.

The facts just stated are potent factors in realizing Earnings which the Santa Fe, per mile operated, increased (Table "E") from $6,298 Gross in 1900 to $10,588 in 1910—equivalent to 68% and in Net from $2,339 per mile to $3,149 or a fraction over 34½%; the L. & N. increased in Gross from $9,226 in 1900 to $11,514 in 1910, or not quite 25%, and in Net from $2,778 to $3,480 or 25¼%.

(Table E.) After giving credit for income from sources other than operation, and after paying interest on the bonded debt, rentals, etc., and dividends, the surplus of the Santa Fe, per mile operated, is $388 less in 1910 than it was in 1900; the surplus of the L. & N. in 1910 is $864 per mile operated more than it was in 1900. Putting it on the eminently proper basis of the Gross Revenue both roads derived from operation, the Surplus (Table "F") of the Santa Fe in 1900 was 14.28% of its gross earnings, and in 1910 had dropped to 4.83%; the surplus of the L. & N. was 5.43% of its gross earnings in 1900 and had increased to 11.85% in 1910.

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With the Santa Fe (Table "E") the interest on bonded debt, rentals, etc., increased per mile operated from $1,048 in 1900 to $1,346 in 1910; dividends increased from $428 to $1,549, or the aggregate total of interest on bonded debt, rentals, etc., and dividends increased per mile operated from $1,476 in 1900 to $2,895 in 1910, equivalent to a fraction less than 100%; the L. & N. reduced its interest on bonded debt, rentals, etc., from $1,791 per mile operated in 1900 to $1,600 in 1910 and increased its dividends from $702 in 1900 to $922 in 1910, or the aggregate total of interest on bonded debt, rentals, etc., and dividends increased from $2,493 in 1900 to $2,522 in 1910, equivalent to less than 1½%, or to be exact 1.16%.

It may be here conceded that the physical condition of the Santa Fe is as adequate to requirements and its service to the public as efficient as that of the Louisville & Nashville.

New Money may and should properly be raised, in the first instance, to construct new mileage in the way of extensions, branches, etc., and such transactions must necessarily rest on their own merits, but one of the main underlying principles evinced by the foregoing comparisons lies, on the one hand, in increasing the efficiency and capacity of any existing plant or business by the numerous means that may be adopted to that end and as may be warranted by its growth out of the resources that, by due caution in all directions, may have been earned and set aside for the purpose, and

on the other hand, by getting the money, very largely, if not entirely, from others, thus incurring the lasting obligations and expense incident thereto, until it is paid back, and to quote Mr. Hines' words: "Every man who reads this will understand how these principles apply to his own business."

It seems clear that Mr. Hines' plea to advance rates, at any rate as a general proposition, is hardly conservative and wise, simply for the purpose of accumulating larger surplus in order to facilitate the raising of funds, either by the sale of additional stock or other unsecured securities, from the proceeds of which the railroads are to protect themselves from depreciation or obsolescence and to extend and improve as the public may demand.

The increased burdens of operation in the way of higher wages, prices, increased expense of public regulation, increased taxes, etc., is another question separate and distinct from it.

Railroads are in fact the property of such of the public as have put their money into them, and in the main that part of the public who utilize them must continue to look to them for the money which may be required in the future, be it new money or money legitimately earned and put aside for Betterments, etc.

Whatever differences exist between the two, or may hereafter arise, must ultimately be adjusted on their merits and merits only, and anything said or done on either side for the sake of expediency can gain no more than a temporary advantage and ever reverts.

As to Capitalization in general: It is to be hoped that the Railway Securities Commission, appointed by President Taft, for the purpose of proposing terms which shall control this feature in future, will reach specific conclusions, fair to all interests involved; but that, it is understood, has no bearing upon what, in this respect, has been done in the past, except perhaps as to roads that may hereafter pass through reorganization processes, and yet it is an issue.

It cannot be gainsaid that under the financing policies which have hitherto prevailed, the outstanding Capitalization of some of our railroads exceeds what they are intrinsically worth from any standpoint, and in briefly reviewing this condition, nothing herein stated is intended as applicable to securities, which stood at their inception and still stand, in their relation to intrinsic values, as gold bricks do to the genuine article.

The past, to which the last few years are no exception, has thoroughly demonstrated that with many roads estimates of future possibilities have not been realized. This is true (1st) of new properties, (2nd) of improvements and extensions to existing lines and (3rd) of estimates of what might be expected of mergers or consolidations of two or more roads by means of reorganization or otherwise. It follows that the securities which were issued, in lieu of the money that was raised to construct new lines or to improve and extend existing ones, and in the matter of mergers or consolidations, partly for like purpose and to complete the consolida-

tions, are to a greater or lesser degree speculative. Apart from that, the intrinsic value of the Securities which had already been issued by existing lines and were outstanding was in a number of cases impaired by the issuance of the new or additional Securities, and in one way or another, the impairment even involves, in some cases, what became underlying bonds upon the completion of consolidation or merger, and to an extent that market values, so-called, are no index to it. The policy pursued is one of the causes that has contributed to the present situation.

It has become pretty plain that the public who utilize the railroads regard it as unjust that rates shall, as a rule, be fixed in relation to existing capitalizations, but it will be found no less unjust to the public who own the railroads that rates shall be fixed, as is urged by many on the other side, on basis of a six or seven per cent. or any percentage return on a capitalization which would represent original cost plus what has since been expended or what the roads may be reproduced for or upon any other like theory, for it will be found that on such a basis, in the very nature of things, the actual physical value of one line, its maintenance, etc., will exceed that of another which directly or indirectly competes with it for all or a vast volume of the traffic; rates that would be fair to one would cripple if not bankrupt the other and would be unjust also to the shipping public who happen to be located on and depended upon roads as last mentioned.

Apparently the travelling public regard passenger rates low enough; at any rate there is little, if any, complaint about them.

According to the latest statistics available, at this writing, the railroads realize on freight traffic as follows:

	An average freight rate in cents, per 100 lbs. of	For an average haul of
In the States of Maine, New Hampshire, Rhode Island and Connecticut	5.1/3	93 Miles
In the States of New York, New Jersey, Pennsylvania, Delaware and Maryland	3.4/5	120 "
In the States of Ohio, Michigan, Indiana, Illinois, Wisconsin	4.1/2	131 "
In the States of Virginia, West Virginia, North Carolina, South Carolina, Georgia, Florida	6.1/5	171 "
In the States of Alabama, Mississippi, Kentucky, Tennessee, Louisiana	6	143 "
In the States of Missouri, Texas, Kansas, Colorado, New Mexico, Oklahoma	9.3/4	183 "
In the States of Iowa, Minnesota, Nebraska, North & South Dakota, Wyoming, Montana	9.1/5	204 "
In the States of California, Oregon, Washington, Nevada, Arizona, Utah, Idaho	10.2/5	191 "

The conditions under which the foregoing rates apply, differ widely in each of the several sections of the country. While it is possible some rates are too high, there is no question but what it can be proven, with reasonable diligent effort before a competent and impartial tribunal, that most of the rates which yield these averages are low in and of themselves and not commensurable to service performed, and on the merits should be advanced.

To proceed on this basis will take care of the increased burdens of operation, and though it is not insured, it may admit of making some return by roads

which, for one reason or another, have not realized results as favorable as others, but it will not yield interest on "gold bricks," and in any event so long as charges in and of themselves are not in excess of the worth of what is exchanged in lieu thereof, no one can be hurt.

Political Economy is still more or less theoretical in its teachings, but it is generally conceded that those of its principles are sound, the practical application of which in the production and distribution of all things possessing exchangeable value work the greatest good to the greatest number; a Government so guided is sound, and these principles are involved in the pending controversy.

The thing of exchangeable value the railroads produce and distribute is transportation, and as a rule it is all they do produce and distribute. It is a potent if not the most potent factor in carrying on the Nation's vast commerce. Unless they get the intrinsic worth of what they produce and distribute, each of those who directly constitute that factor is injured, and amongst these are the individual investors who contributed to the building of the roads in the first instance: the Life Insurance Companies, which have largely invested in railway securities with a view to safeguarding their obligations to hundreds of thousands of their policyholders; the 9,000,000 depositors in Savings Banks, with respect to which the Comptroller of the U. S. Treasury has truly said that "they are part of the

system, the aim of which is a safe and profitable investment of the funds of those who are not so situated as to invest their own money. They are the repositories of the accumulation of wage-earners mainly, and the index to thrift;" likewise the Trust Companies, etc., etc., and the aggregate amount runs into the billions. Apart from all that, railroads are the largest purchasers of raw materials, in the nature of coal as well as manufactures, from locomotives and cars down to a keg of nails, and the most important factors in employing labor. According to the latest authentic statistics, over 7,000,000 persons are engaged in this country in manufacturing and mechanical pursuits; 5,000,000 are engaged in trade and transportation; and nearly 3,000,000 in ordinary labor identified with both these branches of Commerce.

Under our system of Government the people are the arbiters of their own destinies. It seems reasonable to conclude that once the issue becomes clear to the people at large, a fair and permanent solution will be found of the situation which has prevailed, and still prevails, to the detriment of the many.

TABLE "A."

MILEAGE OWNED BY THE TWO SYSTEMS.

	Santa Fe.		L. & N.	
	1900	1910	1900	1910
Mileage owned and operated	7,018	9,931	2,799	4,035
Under construction and completed to June 30/10	...	212	....	....
Owned, but separately operated	352	197	324	269
Total	7,370	10,340	3,123	4,304
As owner of majority of capital stock	....	66	945	1,166
Under joint ownership with other roads	....	563	68	616
Total	....	629	1,013	1,782
Grand total	7,370	10,969	4,136	6,086
Increase, miles	3,598		1,949	
" , %	48.82		45.55	

TABLE "B."

COST OF ROAD AND EQUIPMENT, ACQUISITIONS AND INVESTMENTS.

	Santa Fe.	L. & N.
1900	$407,455,481	$115,151,876
1910	573,431.920	171,127,178
Increase	$165,976,439	$55,975,302
" , %	40.73	48.61

TABLE "C."

CAPITALIZATION OUTSTANDING IN THE HANDS OF THE PUBLIC:

		Santa Fe.	L. & N.
Bonded Debt	1900	$185,466,321	$ 90,378,781
	1910	302,004,953	127,627,500
Preferred Stock	1900	114,182,760	.....
	1910	114,173,730	.....
Common Stock	1900	101,991,100	55,000,000
	1910	165,518,500	60,000,000
Total	1900	$401,640,181	$145,378,781
	1910	581,697,183	187,627,500
Increase, $		$180,057,002	$ 42,248,719
" , %		44.81	29.06

TABLE "D."

EQUIPMENT OWNED, VIZ.:

Locomotives	The Santa Fe owns one to every	5.2 miles operated.
	" L. & N. " " " "	4.9 " "
Passenger Train Cars	The Santa Fe owns one to every	7.2 miles operated.
	" L. & N. " " " "	7.7 " "
Freight Cars	The Santa Fe owns 5.9 cars to every mile	operated.
	" L. & N. " 9.4 " " " "	"

TABLE "E."

THE OPERATING RESULTS, ALL PER MILE OPERATED, WERE:

	1900	1910	Increase. Total.	Increase. %	Decrease. Total.	Decrease. %
Santa Fe. Mileage operated, miles.....	7,341	9,916	2,575	35.08		
L. & N. " " "	3,007	4,554	1,547	51.45		
Santa Fe. Gross Operating Revenue....	$6,298	$10,588	$4,290	68.12		
L. & N. Gross Operating Revenue.....	9,226	11,514	2,288	24.80		
Santa Fe, Operating Exp. and Taxes..	3,959	7,439	3,480	87.90		
L. & N. Operating Exp. and Taxes....	6,448	8,034	1,586	24.60		
Santa Fe. Net Operating Revenue.....	2,339	3,149	810	34.63		
L. & N. " " "	2,778	3,480	702	25.27		
Santa Fe. Income from other Sources...	36	257	221	613.90		
L. & N. Income from other Sources....	216	407	191	88.43		
Santa Fe. Deductions: Fixed Charges, Rentals, etc.....	1,048	1,346	298	28.44		
L. & N. Deductions: Fixed Charges, Rentals, etc.....	1,791	1,600	...	.....	191	10.66
Santa Fe. Dividends paid.....	428	1,549	1,121	261.92		
L. & N. Dividends paid.....	702	922	220	31.34		
Santa Fe. Surplus.....	899	511	...	.....	388	43.16
L. & N. Surplus (Note).....	501	1,365	864	172.46		

NOTE.—During the year 1900 the L. & N. for expenditures for Equipment, Additions and Betterments, charged $1,021,843 to Operating Expenses, equivalent to $339 per mile operated, which, if charged to capital account, as in 1910, would have made L. & N.'s surplus for that year $840 per mile operated, instead of $501.

TABLE "F."

The percentages of "DEDUCTIONS," as shown, to GROSS OPERATING REVENUE are:

	1900 %	1910 %	Increase %	Decrease %
Santa Fe, Deductions: Fixed Charges, Rentals, etc.	16.64	12.71	....	23.62
L. & N. Deductions: Fixed Charges, Rentals, etc.	19.41	13.90	....	28.39
Santa Fe, Dividends paid	6.79	14.63	114.76	....
L. & N. " "	7.61	8.01	5.26	....
Santa Fe, Surplus	14.28	4.83	....	66.18
L. & N. "	5.43	11.85	118.23	....

TABLE "G."

TRAFFIC STATISTICS.

		Santa Fe	L. & N.
(*a*) Freight.			
Density: Revenue tons one mile per mile of road operated	1900	470,589	858,554
	1910	707,230	1,124,075
Average distance hauled, miles	1900	349.19	163.
	1910	360.59	169.76
Average Earnings per ton, $	1900	3.41	1.24
	1910	3.66	1.27
Average Earnings per ton per mile, cts.	1900	0.976	0.758
	1910	1.015	0.751
(*b*) Passenger.			
Density: Passengers one mile per mile of road operated	1900	56,251	73,969
	1910	124,745	104,743
Average distance carried, miles	1900	85.82	35.41
	1910	90.45	43.25
Earnings per passenger, $	1900	1.94	0.818
	1910	1.86	0.979
Earnings per passenger per mile, cts.	1900	2.261	2.310
	1910	2.056	2.263

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